

Message Text

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TAGS: ENRG, TECH, ETRO, EGEN, ECON, EFIN, FI

SUBJ: ENERGY -- IMPACT OF ENERGY SHORTAGE ON

FINNISH ECONOMIC PROSPECTS

STATE ALSO FOR T/IEP

REF: (A) STATE 2951

(B) OECD PARIS 1235

1. SUMMARY: HIGHER COSTS OF OIL RATHER THAN LACK OF
SUPPLIES HAVE CAUSED FINNISH ECONOMIC POLICY MAKERS
TO VIEW FINLAND'S ECONOMIC FUTURE WITH PESSIMISM,
BOTH FOR NEAR AND LONGER-TERM. IN 1974, BALANCE OF
PAYMENTS WILL DETERIORATE SHARPLY; PRICES WILL RISE
AT APPROXIMATELY RECORD RATE OF 1973; EMPLOYMENT WILL
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DETERIORATE IN THE SECOND-HALF; INDUSTRIAL OUTPUT RISE

WILL SLOW DOWN; AND THE GROSS DOMESTIC PRODUCT WILL RISE BY 2.5-3.0 PERCENT IN REAL TERMS COMPARED TO EARLIER PROJECTION OF 4.5 PERCENT. NATIONAL BUDGET WAS PASSED RECENTLY WITHOUT MAKING ANY SPECIAL ADJUSTMENT FOR IMPACT OF OIL CRISIS; THUS, PRESENT FISCAL POLICIES WILL CONTINUE UNCHANGED DURING THE FIRST HALF. SIMILARLY, BANK OF FINLAND WILL CONTINUE ITS RESTRICTIVE MONETARY POLICIES DURING FIRST-HALF TO MINIMIZE DEMAND PRESSURES. END SUMMARY.

2. THE FOLLOWING ECONOMIC ESTIMATES FOR 1974 ARE BASED ON EMBASSY DISCUSSIONS WITH OFFICIALS OF MINISTRY OF FINANCE, BANK OF FINLAND, FEDERATION OF FINNISH INDUSTRIES, AND OIL DISTRIBUTORS:

A. ASSUMPTIONS. OIL SUPPLIES IN 1974 WILL BE ROUGHLY EQUIVALENT TO 1973 LEVEL BUT PRICES WILL RISE BY THREE TO THREE AND ONE-HALF TIMES LEVEL OF LAST YEAR. NEGOTIATIONS WITH SOVIET UNION WHICH SUPPLIES ABOUT TWO-THIRDS OF TOTAL OIL IMPORTS ARE NOW IN PROGRESS. COAL IMPORT PRICES WILL DOUBLE BASED ON RECENT FINNISH-POLISH TALKS, WHICH SOURCE SUPPLIES NEARLY 3.0 MILLION TONS ANNUALLY. EXPORT MARKETS IN EUROPE (PARTICULARLY THE U.K.) WILL HAVE SOMEWHAT HIGHER RATE OF GROWTH THAN RECENTLY ESTIMATED BY OECD (1.5 - 2.0 PERCENT) BUT MARKETS WILL BE DEPRESSED FOR FINNISH PRODUCTS.

B. GROSS DOMESTIC PRODUCT. PREVIOUS GROWTH ESTIMATE OF 4.5 PERCENT PRIOR TO OIL CRISIS WILL HAVE TO BE LOWERED TO 2.5 - 3.0 PERCENT IN 1974. THIS ASSUMES HIGH LEVEL ECONOMIC ACTIVITIES DURING LAST QUARTER 1973 WILL CONTINUE DURING FIRST-HALF, 1974 AND THEN WEAKEN SOMEWHAT IN SECOND HALF. BOTH BANK OF FINLAND AND MINISTRY OF FINANCE OFFICIALS BELIEVE 1975 MAY PROVE TO BE CRUCIAL -- THEY FEAR A FURTHER SLOW-DOWN IN FINNISH ECONOMIC ACTIVITIES.

C. TRADE AND BALANCE OF PAYMENTS. EXPORTS DEVELOPED FAVORABLY IN 1973 PARTICULARLY FOR PAPER LIMITED OFFICIAL USE

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AND OTHER FOREST-BASED PRODUCTS; THIS WILL CONTINUE IN 1974. CONSUMER PRODUCTS SECTOR HOWEVER WILL HAVE DIFFICULTY EXPANDING SALES. TERMS OF TRADE OVERALL WILL DETERIORATE 4.0 - 8.0 PERCENT LARGELY BECAUSE OF HIGHER OIL IMPORT COSTS -- THIS ASSUMES IMPORT PRICES OF RAW MATERIALS WILL RISE ON AVERAGE NEARLY ONE-THIRD WHILE EXPORT PRICES WILL GO UP NEARLY ONE-FOURTH. OIL IMPORT COSTS WILL RISE

FROM FMK 1.7 BILLION IN 1973 TO WELL OVER FMK 5.0 BILLION IN 1974 WITHOUT CHANGE IN VOLUME. BY VOLUME, TOTAL IMPORTS SHOULD HOLD AT 1973 LEVEL WHILE EXPORTS WILL GO UP ABOUT 4.0 PERCENT. NO FIRM ESTIMATE IS POSSIBLE OF BALANCE OF TRADE OR PAYMENTS DEFICIT THIS YEAR BUT TRADE DEFICIT OF FMK 1.9 BILLION IN 1973 WILL MOST LIKELY DOUBLE WHILE PAYMENTS DEFICIT WILL RISE FROM FMK 1.4 - 1.5 BILLION IN 1973 TO AT LEAST FMK 2.7 BILLION. MUCH OF DEFICIT WILL BE WITH SOVIET UNION WITH WHICH FINLAND HAS BILATERAL ARRANGEMENT. TALKS HAVE BEEN HELD TO INCREASE FINNISH EXPORTS TO SOVIET UNION TO OFFSET HIGHER OIL IMPORT COSTS BUT THIS WILL NOT LEAD TO NARROWING TRADE GAP APPRECIABLY IN 1974. BIG QUESTION IS WHETHER SOVIET UNION WILL BE WILLING TO EXTEND "FREE CREDIT" UNTIL FINLAND CAN MAKE UP DEFICIT.

D. PRICES. IN 1973, COST-OF-LIVING AND CONSUMER PRICES ROSE BY 15.3 PERCENT BETWEEN JANUARY AND DECEMBER WHILE WHOLESALE PRICES ROSE BY EVEN MORE. BASED ON ANTICIPATED COST AND DEMAND PRESSURES, CONSUMER PRICES IN 1974 WILL RISE BY A MAGNITUDE SIMILAR TO 1973 EVEN IF THERE IS A FAVORABLE OUTCOME OF WAGE AND INCOMES POLICY NEGOTIATIONS LIMITING NOMINAL WAGE INCREASE TO ROUGHLY TEN PERCENT PLUS BENEFITS FROM TAX REDUCTIONS (FMK 400 - 1,000 MILLION) AND OTHER FRINGE IMPROVEMENTS.

E. CONSUMPTION AND EMPLOYMENT. CONSUMPTION LEVEL IS ESTIMATED TO DECLINE SOMEWHAT FROM 1973 ASSUMING WAGE SETTLEMENT DESCRIBED ABOVE. AT PRESENT, EMPLOYMENT IS HIGH AND UNEMPLOYMENT RATE IS ROUGHLY 2.0 PERCENT. BUT THIS IS EXPECTED TO DETERIORATE LIMITED OFFICIAL USE

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SHARPLY IN SECOND-HALF TO MORE THAN 3.0 PERCENT (POSSIBLY 3.3 PERCENT BY END OF YEAR). INCREASED BUDGETARY EXPENDITURES FOR PUBLIC WORKS TYPE ACTIVITIES PLUS UNEMPLOYMENT BENEFITS WILL BE REQUIRED. THIS DEVELOPMENT ASSUMES A DETERIORATION IN TERMS OF TRADE AND COST PRESSURES ON INDUSTRY AND BUSINESS CAUSING RELEASE OF WORKERS.

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F. INDUSTRIAL OUTPUT. OUTPUT PROJECTIONS WILL HAVE TO BE LOWERED FROM THE EARLIER 6.0 PERCENT TO PERHAPS 4.0 PERCENT COMPARED TO 1973 AVERAGE. OUTPUT ESTIMATES ARE GARBLED BY FACT STATISTICAL BUREAU STATISTICS SHOW ONLY 3.0 PERCENT RISE IN 1973 BUT THIS FIGURE PROBABLY UNDERESTIMATES REAL INCREASE BY VERY SUBSTANTIAL AMOUNT, JUDGED BY NATIONAL INCOME AND ELECTRICITY USE FIGURES. FOR EXAMPLE, MINISTRY OF FINANCE ESTIMATES INDUSTRIAL OUTPUT ROSE IN 1973 BY 6.0 - 7.0 PERCENT. PRIVATE INVESTMENT ACTIVITIES ARE EXPECTED TO RISE ABOUT 4.0 - 5.0 PERCENT IN 1974, GIVING A BOOST TO OTHERWISE DISMAL DEMAND PROSPECTS. THIS ESTIMATE IS BASED ON EVIDENCE OF HIGHER PROPENSITY TO INVEST JUDGING FROM RECENT FEDERATION OF FINNISH INDUSTRIES SURVEY, WHICH WAS CONDUCTED FOLLOWING SIGNING OF EC AGREEMENT. OIL

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CRISIS COULD REDUCE SOMEWHAT INVESTMENT ACTIVITIES BUT SINCE ROUGHLY 70 PERCENT OF INDUSTRY IS NOW OPERATING

AT OR NEAR CAPACITY LEVELS THERE IS A STRONG DEMAND.

G. FISCAL AND MONETARY POLICIES. IN RECENTLY PASSING NATIONAL BUDGET OF FMK 17.2 BILLION, QUESTIONS WERE RAISED ON ITS FAILURE TO TAKE INTO ACCOUNT THE OIL CRISIS BUT NO SUBSTANTIAL CHANGE WAS MADE TO ORIGINAL BUDGET. GOVERNMENT POSITION, WHICH WAS ACCEPTED, WAS THAT OIL IMPACT WILL HAVE TO BE CONSIDERED IN SUPPLEMENTARY BUDGETS. PRESENT POSTURE THEREFORE IS FOR NO NEW INITIATIVES IN FISCAL FIELD IN FIRST-HALF. FOR MONETARY AREA, CURRENT RESTRICTIVE POLICIES WILL BE CONTINUED, ACCORDING TO BANK OF FINLAND SOURCE. IN FACT, EFFECTIVE JANUARY 23 BANK OF FINLAND EASED QUOTA FIGURE FOR COMMERCIAL BANKS SEEKING REDISCOUNT ACCOMMODATIONS BUT PLACED A CEILING ON TOTAL AMOUNTS THAT CAN BE REDISCOUNTED BY COMMERCIAL BANKS. MOREOVER, LOANS OBTAINED BY USE OF GOVERNMENT BONDS WILL RISE TO 26 PERCENT ANNUAL RATE, DOUBLE CURRENT RATE.

3. COMMENTS: THERE IS CONTROVERSY AS TO WHETHER ENERGY CRISIS WILL AFFECT FINLAND MORE ADVERSELY THAN OTHER EUROPEAN COUNTRIES BUT IT IS CLEAR THAT IRRESPECTIVE OF THIS, FINLAND WILL BE REQUIRED TO TIGHTEN ITS BELT TO MEET THE HIGHER OIL IMPORT COSTS AND WILL BE SEEKING NEW LOANS, HOPEFULLY LONG-TERM, DURING THE COURSE OF THE YEAR. SUGGESTIONS HAVE BEEN MADE THAT SUCH LOANS BE OBTAINED FROM THE ARAB WORLD BUT WHETHER THIS WILL BE POSSIBLE IS NOT KNOWN. IN THE MEANTIME, THE GOVERNMENT HAS MADE PREPARATIONS FOR POSSIBLE RATIONING OF OIL USE, POSSIBLE FURTHER USE OF PRICE CONTROL AUTHORITY, AND OTHER MEASURES TO MAINTAIN ECONOMIC STABILITY. FOR LONGER-TERM THERE ARE SUGGESTIONS ALSO THAT FINLAND WILL BE REQUIRED TO DEVALUE THE FINNMARK. TWO ATOMIC ELECTRIC GENERATING PLANTS (AT KOPPARNAS AND OLKILUOTO) PLANNED BY IMATRAN VOIMA OY WERE GIVEN OFFICIAL APPROVAL BY THE GOVERNMENT AND ANNOUNCED YESTERDAY WHILE PLANS FOR ADDITIONAL PLANTS IN THE COMING YEARS ARE LIKELY TO LIMITED OFFICIAL USE

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